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From: Bill Gates
Sent: Tuesday, December 01, 1998 7:13 AM
To: Executive Staff
Subject: AOL-NSCP and why consumers shouldn't pay for browsers

A lot of people have asked me about the AOL/Netscape merger. It's certainly paradoxical, given the DOJ case.

The DOJ must be VERY dismayed at this merger.

It will finally make people question why the DOJ is trying to raise the price of browsers above the competitive price, which is zero. It will finally make people question why the DOJ is attacking the browser work we did that benefited consumers through integration and innovation. Like almost all browser software, AOL's access software has always been free. AOL will distribute Netscape browser software for free to its 20 million instant messaging customers, and sooner or later to all its online service customers too. Our work in browsers made the business more competitive and consumers clearly benefited as browsers became free as they should be (and as they used to be, before Netscape gained a big share).

We decided a long time ago that Web browsing software should be part of a modern, well-designed operating system - this approach benefits consumers by giving them a single, simple interface through which to access all types of information, and by making it easier to use the Web with other applications. We also decided that, just like the many other features that are now built into Windows, there would be no extra charge for our browser technology. That makes business sense - one payoff for Microsoft comes through making Windows even more appealing to consumers. Just as consumers now prefer their car to come with an integrated, easy to use audio system, most want their PC operating system to include integrated, easy to use Web browsing technology.

Why is Netscape worth \$4 billion despite making its browser available for free? The answer is that browsers - whether they come as part of an OS or standalone - generate so much advertising revenue that you maximize revenue by giving them away free to drive usage. Jim Clark remembers that I made this point and the point about integration in the Fall of 1994, before Netscape came out with their first product. If there is competition the price will be zero. Browsers are like network TV. The traffic alone makes it a great business to make a popular browser even without charging users. There is nothing predatory about pricing a product at a profitable price. In fact, it's called the marketplace at work, and it helps consumers.

Netscape and now AOL has an incredible ability to get its product into the market, including the use of the Internet itself. No one has "foreclosed" Netscape from distributing its software. Netscape's success is proof of how open the software industry is to new competition. In how many segments of the economy can a startup grow to a market valuation of \$4 billion in only four years?

Yet the claim that Netscape was "foreclosed" from distributing its software is not just the center of the DOJ case - it IS the DOJ case.

The history here is very instructive. When we first included browser capabilities in Windows they did not get much use. Netscape continued to have over 80% share and



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there was no pressure on its price. Only when our browser won the overwhelming majority of all reviews did our share move up and Netscape have to come back down to a competitive price. It took a great deal of innovative work for us to not only catch up but move ahead in the browser business and we can be very proud of our contributions on behalf of consumers.

Microsoft's inclusion of Internet standards in Windows was pro-competitive. Imagine how people would have reacted if we had NOT included Internet standards like TCP/IP or HTML in Windows. Our old "help" format was proprietary and we got rid of it. Our track record of working with the standards group on HTML is the best of any company.

The ironies in this case are quite amazing. The DOJ meets with our competitors in their homes, and at dinners with all of our competitors present, and discusses what they can do against us. Perhaps these cozy relations will make it easier for AOL to get mergers such as Mirabilis, CompuServe and Netscape approved. The DOJ hasn't seemed to notice that the #1 gateway to the Internet (AOL) bought the #2 gateway to the Internet (CompuServe), and raised prices immediately following government approval of the merger. The DOJ hasn't seemed to notice that our business is more competitive than ever with many strong attacks on the Windows business.

The company that helped make sure consumers got a fair price for browsers has the DOJ attacking it on behalf of the company that did not.

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